BRIEF IN SUPPORT OF PETITION.

OPINIONS BELOW.

The opinion of the Circuit Court of Appeals, for a review of which the petition herein is filed, appears on page 250 of the record. It is not yet reported. The previous opinion of the Circuit Court of Appeals in litigation between the same interests, over the same subject-matter, appears as an appendix to this brief.

JURISDICTION.

Basis upon which it is contended this court has jurisdiction to review is stated in the petition (*ante*, p. 3).

QUESTIONS PRESENTED.

The questions presented are stated in the petition (*ante*, p. 2).

REASONS FOR ALLOWANCE OF WRIT.

The reasons for allowing the writ are stated in the petition (*ante*, p. 8).

STATEMENT.

A statement of the case is in the petition (*ante*, p. 4).

STATUTES INVOLVED.

The West Virginia statute involved is referred to and quoted from in the petition (*ante*, p. 4).

ARGUMENT.

Point I.

IN THE FIRST CASE, WHERE THE MINORITY SOUGHT TO ENJOIN THE DISSOLUTION AND SALE, THE AFFIRMANCE BY THE CIRCUIT COURT OF APPEALS OF THE DISTRICT COURT DECREE WHICH DISMISSED THE MINORITY'S BILL ON THE GROUND THAT THE PROPOSED DISSOLUTION, SALE AND PURCHASE WERE NOT FRAUDULENT WAS NECESSARILY A HOLDING THAT SUCH PROPOSED ACTION WAS NOT FRAUDULENT, WHICH IS DIRECTLY IN CONFLICT WITH THE SAME COURT'S DECISION IN THE MINORITY'S SUBSEQUENT DAMAGE SUIT WHICH HOLDS THAT THE SALE AND PURCHASE MADE EXACTLY AS CHARGED IN THE FIRST CASE WERE FRAUDULENT.

The conflict is between the decisions in *Lebold, et al.* v. *Inland Steamship Company*, 82 Fed. (2d) 351 (Appendix to this petition), and *Lebold, et al.* v. *Inland Steel Company*, a subsequent phase of the same controversy. (The instant case, not yet reported, but found at Rec. p. 250.) In the first opinion the Circuit Court of Appeals necessarily decided that the contemplated dissolution and sale were not fraudulent or improper. In the second opinion the same court held that the dissolution and sale, which were carried out exactly as the first case charged they would be, was fraudulent and improper.

When a meeting was called to dissolve Steamship Company, the minority filed a bill to enjoin the dissolution charging that Steel Company intended to acquire complete ownership of the assets of Steamship Company by purchasing them at the dissolution sale, and intended to continue to operate said assets for its own purposes in the same manner that they had been theretofore operated, and that this would amount to a continuance of the business of Steamship Company by Steel Company. (Rec. 143-146.)

In its answer and in its testimony defendant admitted that it intended to purchase the ships, if no one bid an amount higher than their agreed physical asset value (which was very unlikely because of the depression), and that, if purchased, it would employ them to carry the freight of Steel Company as theretofore. (Rec. 158, 55.) The District Court dismissed the bill for want of equity and specifically held that the contemplated dissolution and sale was not fraudulent or improper and that Steel Company might bid for the ships at the sale. (Rec. 168-170.) Upon appeal the Circuit Court of Appeals affirmed the lower court in its dismissal of respondents' bill for want of equity, but held that the affirmance would be without prejudice to a subsequent presentation of the same facts in connection with *such further facts*, if any, as might bring about a situation within the doctrine recognizing causes of action in minority stockholders. (Appendix, p. ix.) It held that the majority might proceed to a dissolution but that what would happen then or thereafter was not then before the court and could not then be made the basis for a finding of fraud. It held that the bill was premature and that the court below rightfully held that the evidence did not make out a case within the legal principles which it had outlined in its opinion. (Appendix, p. vi.)

Respondents would undoubtedly concede that if the court had affirmed the District Court without qualification, such affirmance would necessarily have amounted to a holding that the contemplated dissolution sale and purchase was not a fraud upon the minority, a holding directly at variance from that now announced by it. It is merely because the court attempted to qualify its affirmance, as noted above, that respondents contend that the two decisions are not in conflict. We respectfully submit that the conflict cannot be thus avoided. The injunction sought to enjoin an alleged threatened fraud. The injunction suit sought to prevent not only the dissolution but also the

sale of the ships, their purchase by Inland Steel Company, and their use by that company for the purpose of carrying its own freight. This is disclosed not only by the bill and its prayer, but by the terms of the temporary restraining order obtained without notice. (Rec. 145, 146, 148.) The parties and the court knew that if there was a dissolution there would necessarily be a sale. They knew that the depression had so affected the steel industry that there was no market for lake freighters and that Steel Company would undoubtedly be the purchaser. (Rec. 194-5, 55.)

It is undeniably true that if the course which Steel Company admitted it intended to pursue was fraudulent, the court had clear jurisdiction to enjoin it. As this court has said in *Swift and Company* v. *U. S.*, 276 U. S. 311, 326:

> "* * * a suit for an injunction deals primarily, not with past violations, but with threatened future ones; and * * * an injunction may issue to prevent future wrong, although no right has yet been violated."

See also, *Carter* v. *Carter Coal Co.*, 298 U. S. 281, 287-288; *Pierce* v. *Society of the Sisters*, 268 U. S. 510, 536; *Pennsylvania* v. *West Virginia*, 262 U. S. 553, 592-593; and *Vicksburg Waterworks Co.* v. *Vicksburg*, 185 U. S. 65, 82.

The Circuit Court of Appeals (on the record having no choice but to believe that defendant intended to do what it said it was going to do) would necessarily have reversed the lower court and ordered the injunction to issue if it had been of opinion that such actions would be fraudulent or improper.

A dismissal "without prejudice" does not permit the relitigation of issues then before the court. *State of Missouri* v. *Chicago, Burlington & Quincy R. R.*, 241 U. S. 533, 539; *Arkadelphia Co.* v. *St. Louis Southwest Ry. Co.*, 249 U. S. 134, 147; *Window Glass Machine Co.* v. *New Bethlehem Window Glass Co.*, 264 Fed. 822 (3 C. C. A.);

Window Glass Mach. Co. v. *New Bethlehem Window Glass Co.*, 269 Fed. 979 (3 C. C. A.).

The plan to dissolve the corporation and to buy the ships was the plan that was under attack in the first case. The affirmance by the lower court placed its stamp of approval upon that plan and removed it from further inquiry. The ruling by the Circuit Court of Appeals that its affirmance of the lower court's decree would be regarded as without prejudice, left open to plaintiffs only the right to attack fraud if any that occurred subsequent to the dissolution in a sale different from that proposed, as, for instance, a sale for an inadequate price, or an inequitable distribution of the proceeds of the sale. It is highly significant to note that in the extensive *obiter dicta* indulged in by the Circuit Court of Appeals in its first opinion, after deciding to affirm the lower court, it did not indicate that if the dissolution and sale were carried out as proposed, it would hold the same to be a fraud. The court could have said that very easily and plainly had it meant it. On the contrary, after having ruled that a holder of 60% of the capital stock has a right to dissolve a corporation regardless of motive or expedience (Appendix, p. v, l. 8) and, inferentially, that a sale by the majority to itself at full value would be proper (Appendix, p. v, l. 30) it merely indicated *obiter* a fear that the majority would "force dissolution and liquidation of assets and thus produce an opportunity to purchase at a satisfactorily low market price all the physical assets." (Appendix, p. viii.)

II.

THE CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT HAS HELD THAT IT IS A FRAUD ON THE MINORITY FOR A PARENT COMPANY TO PURCHASE THE ASSETS OF ITS SUBSIDIARY, AT THE DISSOLUTION SALE, FOR A FULL FAIR PRICE. THIS IS CONTRARY TO THE HOLDING OF THE CIRCUIT COURT OF APPEALS IN THE FIRST CIRCUIT IN A SIMILAR SITUATION.

It is very important to note:

1. Steamship subsidiary had always been merely an instrumentality of Steel Company, used by the parent corporation to transport its ore, limestone and coal. (Rec. 192.)

2. No peculiar value inhered in the ships. They were ordinary Great Lakes freight carriers, of which there was an over-supply and for which there was no demand because of the depression in the steel trade. (Rec. 193, 195.)

3. The price paid for these ships at the dissolution sale was a full fair price. (Rec. 208.)

4. It was stipulated that there was no contractual arrangement of any kind that made it necessary for Steel Company to continue to use the services of Steamship Company and therefore its relationship to Steel Company created no transferable intangible asset of value. (Rec. 194.)

This was not the kind of a case which, as the Court seems to have thought (Rec. 258) would have been presented if Henry Ford dissolved the Ford Company and attempted to settle with his minority stockholders on a physical asset basis. Such a transaction would have been improper for the reason that there is more to the Ford Company than physical assets. It has good will, valuable patent rights, established custom and valuable outlets protected by contract. The case decided by the Court was analogous to a situa-

tion where the Ford Company owning eighty per cent of the stock of a subsidiary auto-truck company that did its hauling *without a contract* in a fleet of Ford motor trucks, dissolved the subsidiary and bought the trucks at the dissolution sale for a fair price, and used them thereafter for its own hauling.

It is clear that the Circuit Court of Appeals has held that Steel Company defrauded the minority merely because it purchased the ships at the dissolution sale. Under the opinion Steel Company would not have been held to have done any wrong (a) if the ships had been sold to third parties; (b) if the ships had been sold to third parties and Steel Company had thereupon purchased other ships to carry its own property; (c) if Steel Company had purchased the ships, but had used them to haul the freight of other persons, and had bought additional ships to haul its own freight; or (d) if a third party had purchased the ships and Steel Company thereupon had purchased them from such third party, and used them to haul its freight. In each instance Steamship Company in liquidation would have received no greater price for the ships than it did in fact receive, and would have received nothing for its "business" because it had no "business" to transfer.

If it was right for the Steel Company to buy the ships, it certainly could not have been wrong for it to use them to transport its own property which it was not obligated to permit anyone else to transport. Therefore, no matter how the situation is viewed, the alleged wrong consisted only of the purchase of the ships by the parent company at the dissolution sale.

In *May* v. *Midwest Refining Co., et al.* (C. C. A. 1st, June 6, 1941), 121 Fed. (2d) 431, 439, Standard Oil Company acquired a substantial majority of the stock of Midwest Refining Co., a Maine corporation, the statutes of which State permitted majority stockholders to liquidate the corporation over the protest of a minority, just as do

the statutes of West Virginia. Standard Oil Company voted to purchase the properties for itself. The court held that even though Standard Oil Company might be regarded as a trustee by reason of its alleged domination and control over Midwest Refining Co., nevertheless it had a right to purchase the assets of its subsidiary for a fair price, although the transaction called for rigorous scrutiny because of the relationship of the two companies. It cited *Pepper* v. *Litton*, 308 U. S. 295, 306; 60 S. Ct. 238, in support of its ruling.

III.

IT IS IN CONFLICT WITH LOCAL WEST VIRGINIA DECISIONS FOR THE CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT TO HOLD THAT WHEN A MAJORITY STOCKHOLDER OF A SOLVENT PROSPEROUS WEST VIRGINIA SUBSIDIARY VOTES IN ITS OWN INTEREST AND AGAINST THE INTERESTS OF THE MINORITY STOCKHOLDERS OF SUCH SUBSIDIARY, TO DISSOLVE IT AND PURCHASE SUCH SUBSIDIARY'S PHYSICAL ASSETS AT THE DISSOLUTION SALE, THE MAJORITY STOCKHOLDER COMMITS A BREACH OF TRUST AND A FRAUD ON SUCH MINORITY STOCKHOLDERS.

It is clear that if a parent corporation's purchase of its solvent subsidiary's assets for a fair price at a legal dissolution sale, and their use in the parent corporation's business is to be regarded as a fraudulent usurpation, reorganizations are at the mercy of a protesting minority, which is a reversion to the doctrine of the common law long since discarded or abrogated by statutes such as that of West Virginia. The question is of especial importance when, as here, and as is very frequently the case, the subsidiary is merely an instrumentality in the service of the parent corporation and the parent corporation is not only the natural purchaser, but the only available one. The decision of the Circuit Court of Appeals in the instant case is in conflict with the West Virginia case of *Tierney* v. *United Pocahontas Coal Co.*,

85 W. Va. 545, 559, 102 S. E. 249, 255 (1920), where the majority forced the sale of the property of its subsidiary to itself, and the court said:

> "If such a transaction is entirely fair, and prejudices the rights of no interested party, there is no reason why it should not be upheld, as well as such a sale to an entirely disinterested party, and it may be said in passing that a reasonable test to be made of the fairness of such a sale is: Would the proposition from one disconnected with the whole affair have been accepted by those acting for the selling company?"

The Circuit Court of Appeals has held that a majority stockholder commits a breach of trust when it votes in its own interest and against the interest of the minority. (Rec. 253.)

It is of controlling importance to notice that it is the stockholders and not the directors who vote on the question of the dissolution of a West Virginia corporation. Steel Company voted the dissolution through its duly authorized representatives. (Rec. 172.) The directors of Steamship Company had no vote.

For reasons valid, but immaterial, since the majority may accomplish dissolution of a West Virginia corporation regardless of motive or expediency (Appendix, p. v), Steel Company wished to carry its iron ore, limestone and coal in its own ships instead of in those of a subsidiary. One way to accomplish this was to dissolve the subsidiary and purchase the ships at a fair sale. The other way was to buy other ships and leave the subsidiary with its ships. In the latter case, as respondents have stipulated, there would have been no freight for Steamship Company to carry. (Rec. 196, par. 23.) In either case the minority stockholders would cease to receive the large profits which they had been enjoying solely out of the carriage of Steel Company's freight. It is respectfully submitted that Steel Company was not bound to use

Steamship Company as its freight carrier forever and could vote in its own interest to dissolve its subsidiary in spite of the fact that this was detrimental to the minority stockholders. The Circuit Court of Appeals has held that it could not carry out its dissolution plan because a vote by a majority stockholder detrimental to the interests of the minority stockholders constitutes a breach of trust. (Rec. 253.) We submit that such holding is contrary to the holding of the Supreme Court of West Virginia in *Thurmond* v. *Paragon Colliery Co.*, 82 W. Va. 49, 53, 95 S. E. 816, 817 (1918), where the court, in speaking of the vote of stockholders, as distinguished from those of directors, said:

> "The reason for denying to a director of a corporation the right to vote on a matter in which he is otherwise interested, than as a stockholder in the corporation, is because of the fiduciary or trust relation he bears toward it. 4 Thompson on Corporations, Sec. 4467. But that reason does not apply to a stockholder, and he is not denied his right to vote on any matter properly coming before a stockholders' meeting on account of any private interest he may have which is detrimental to the corporation. 4 Thompson on Corp., Sec. 4467; *Shaw* v. *Davis*, 78 Md. 308, 28 Atl. 619, 23 L. R. A. 294; *Windmuller* v. *Standard Distilling & Distributing Co.* (C. C.) 114 Fed. 491. In *Gamble* v. *Queens County Water Co.*, 123 N. Y. 91, 25 N. E. 201, 9 L. R. A. 527, it was held:
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> > 'A shareholder has a legal right, at a meeting of the shareholders, to vote upon a measure even though he has a personal interest therein separate from other stockholders. In such a meeting each shareholder represents himself and his own interests solely, and he in no sense acts as a trustee or representative of others.' "

The Circuit Court of Appeals has cited *Pepper* v. *Litton*, 308 U. S. 295, 306; 60 S. Ct. 238, to demonstrate (a) that a parent corporation, dominant stockholder in its subsidiary,

is a fiduciary when it assumes control, a principle which petitioner is not controverting, and (b) that *in spite of the West Virginia Statute* it is *ipso facto* a breach of trust for such parent corporation to vote for the dissolution of its subsidiary against the interests of the minority stockholders thereof and to purchase the subsidiary's physical assets for a full fair price and use them in its business, a holding which we respectfully submit *Pepper* v. *Litton* does not stand for in any sense.

IV.

THE QUESTION OF LIABILITY TO ACCOUNT WAS THE ONLY QUESTION BEFORE THE CIRCUIT COURT OF APPEALS, BUT IN REVERSING THE CASE IT WENT BEYOND THAT QUESTION AND LAID DOWN A RULE OF DAMAGES, ALTHOUGH THE QUESTION OF THE MEASURE OF DAMAGES, IF THERE WAS LIABILITY, HAD NEVER BEEN ARGUED.

The case had been referred to a Master "solely upon the issue as to whether or not plaintiffs are entitled to an accounting from defendant". (Rec. 37.) The Master stated they were not so entitled. The District Court affirmed the Master. Now, in reversing the District Court, the Circuit Court of Appeals has held the defendant liable to account to plaintiffs, and has laid down the rule of damages which should be applied to that accounting, and has even roughly sketched out the maximum and minimum amounts of damages which it announces plaintiffs are entitled to recover. In the injunction suit respondents (plaintiffs) introduced evidence as to the value of their stock, to demonstrate that the $700 per share offered by Steel Company for it was not "going concern" value. Defendant introduced countervailing testimony to show that the absence of contractual relations between the two companies and the dissolution removed "going concern" value from consideration, but nowhere was the issue raised as to what the measure of damages would be in the event

an accounting was ordered. Regardless of this, the Circuit Court of Appeals has held that the Steel Company had a right to dissolve the Steamship Company, but that when it did so, and purchased the ships for their full fair value instead of letting them disintegrate at the dock for want of a purchaser, it became liable in damages to the minority just as though it had converted the minority's interest to its own use; that it became liable to pay in one lump sum the capitalized value of the earnings of the company, that is to say, the same amount which the minority would have received over an indefinite period of years as dividends if the Steamship Company had not been dissolved and was not going to be dissolved, but was going to continue in business until the expiration of its charter. We respectfully submit that defendant was entitled to be heard on the question of the correctness of this drastic rule of damages announced for the first time in the court's opinion, and that the court, in deciding that question without a hearing, has so far departed from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision.

Petitioner respectfully submit that the writ of certiorari should issue.

Respectfully submitted,

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